Service Date: June 8, 1984

DEPARTMENT OF PUBLIC SERVICE REGULATION
BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MONTANA

IN THE MATTER of the Application of PACIFIC POWER AND LIGHT COMPANY for Authority to Increase Rates and Charges for Water Service to its Consumers in its Libby, Montana Service Area.	DOCKET NO. 83.8.59 ORDER NO. 5064

APPEARANCES

FOR THE APPLICANT:
John Dudis, Attorney at Law, Murphy, Robinson, Heckathorn and Phillips, One Main Building, Kalispell, Montana 59901.
Nancy Ganong, Attorney at Law, Stoel, Rives, Boley, Fraser and Wyse, 900 S.W. Fifth Avenue, Portland, Oregon 97204.

FOR THE INTERVENOR:

James C. Paine, Montana Consumer Counsel, 34 West Sixth Avenue, Helena, Montana 59620.

FOR THE COMMISSION:
Calvin Simshaw, Staff Attorney, 2701 Prospect Avenue, Helena, Montana 59620.

BEFORE:
Howard Ellis, Commissioner and Hearing Examiner

BACKGROUND

1. On August 26, 1983, Pacific Power and Light Company (Applicant or PP&L) filed an application with this Commission for authority to increase rates and charges for water service at Libby, Montana. The Applicant requested an average increase of approximately 28.5%, which constitutes an annual revenue increase of approximately $136,417.

2. Concurrent with its filing for a permanent increase in rates, PP&L filed an application for an interim increase in rates of approximately 16.3% equaling a revenue increase of approximately $78,131.

3. The Commission, because of an administrative oversight by its staff, never took action on the Applicant's request for interim rate relief and at the close of the public hearing in this Docket, the Applicant withdrew its request for interim rate relief.

4. On February 7, 1984, pursuant to Notice of Public Hearing, a hearing convened in the Courthouse, County Annex Building, Libby, Montana. The purpose of the hearing was to consider the merits of the Applicant's proposed water rate adjustment. At the close of the public hearing, all parties waived their right to a proposed order and stipulated to authorize the Commission to issue a final order in this Docket. Section 2-4-622, MCA.

ANALYSIS AND FINDINGS OF FACT

5. The Applicant presented the testimony and exhibits of the following witnesses:

Wayne Goin, Vice President and Division Manager
Robert L. Svendsen, Senior Water System Engineer:
Donald C. Lamb, Cost of Capital Supervisor
Robyn A. Warsinske, Rate of Return Analyst
A. Brooks Congdon, Cost of Service Analyst
Lyle W. Kammerer, Rate Analyst

6. The Montana Consumer Counsel presented the testimony of sixteen public witnesses at the hearing. The testimony of these witnesses was generally in opposition to the rate increase, and also focused on the area's economic condition, the fact that the system is gravity-flow, effect of rate increases on fixed income customers, maintenance policies and the effect of sprinkling rate increases on lawns and gardens.

7. The test year ending December 31, 1982, as proposed by the Applicant, was uncontested and is found by the Commission to be a reasonable period within which to measure Applicant's utility revenues, expenses and returns for the purpose of determining a fair and reasonable level of rates for water service.

8. The Libby water utility is one of a number of regulated

utilities within the corporate structure of PP&L under this Commission's jurisdiction. Therefore, certain issues impacting ratemaking for the water utility have been addressed in prior proceedings before the Commission. Issues such as, but not limited to, capital structure, cost of debt, cost of equity and composite cost of total capital are elements common to all of the regulated utilities within the corporate structure of PP&L, under this Commission's jurisdiction. On February 8, 1984, this Commission issued Order No. 5009a for PP&L's Montana electric service. This Order had the effect of resolving certain ratemaking issues which are common to PP&L's utility operations in Montana.

9. PP&L at the start of the public hearing in Libby, revised its requested revenue increase. The revised revenue increase results from PP&L's incorporation of findings, on common issues, from this Commission's Order No. 5009a which impact the water utility. After recognizing the impact of the findings from the electric order, the Company's requested annual revenue increase drops from $136,417 as filed to $69,063 as revised (Late - Filed Ex. 2L, p. 1 of 31).

RATE BASE

10. The Applicant proposed an average original cost depreciated ratebase of $1,812,500. The rate base proposed by the Applicant was not challenged by any party participating in this proceeding and, therefore, is accepted by the Commission.

CAPITAL STRUCTURE AND ASSOCIATED COSTS

11. The Applicant, in its application, proposed the following capital structure and associated costs:

Description	Capital Structure	Cost	Weighted Cost
Long-Term Debt	52.0%	10.19%	5.30%
Preferred Stock	12.0	10.9	1.32
Common Equity	36.0	17.10	6.16
Weighted Total	100.0%		12.78%

12. As stated previously, the Commission issued an order for PP&L's Montana electric operations on February 8, 1984.
With regard to capital structure and associated costs, that order specified the use of the Applicant's actual, capital structure, cost of long-term debt and preferred stock cost as of August 31, 1983 (excluding the impact of the debt/equity exchanges and the Company's investment in subsidiaries). The order further provided that the Applicant be allowed a 13.75% return on common equity.
The Applicant, at the public hearing, proposed adoption of the 13.75% common equity return and the methodology employed by the Commission in the electric order for purposes of determining capital structure and cost rates on long-term debt-and preferred stock. The Applicant also proposed that it be allowed to update the Company's long-term debt and preferred stock costs and actual capital structure to the November 30, 1983 level.

13. The fact that the Libby water utility is one of a number of regulated utilities within the corporate structure of PP&L means that common issues, such as capital structure and associated costs, which have been addressed in prior Commission proceedings should be given similar treatment for ratemaking purposes. Therefore, the Commission finds that use of the actual capital structure and associated costs and the 13.75% return on common equity as specified in Order No. 5009a is acceptable.

14. Relative to allowing the Applicant to update capital structure and costs to November 30, 1983, the Commission has consistently viewed updating as a positive way of more accurately portraying known and measurable capital costs and, therefore, accepts the use of actual data as of that date.

15. The Commission finds the following capital structure and cost of capital to be appropriate:

Description	Capital Structure	Cost	Weighted Cost
Long-Term Debt	58.0%	9.76%	5.66%

Preferred Stock	13.0	10.00	1.30
Common Equity	29.0	13.75	3.99
Weighted Total	100.0%		10.95%

OPERATING REVENUE

16. The test period operating revenues are not a contested issue in this case. The Applicant utilized a 12-month period ending December 31, 1982, to determine test year revenues under the rates which became effective June 3, 1983. Total test year revenues of $478,763, as calculated by the Applicant, are accepted by the Commission.

OPERATING EXPENSES

17. The Applicant has the following revised proforma expenses reflecting adjustments from Order No. 5009a, impacting the water utility, and a 10.95% overall rate of return.

Operation and Maintenance Expense	$197,174
Depreciation	43,557
Taxes Other Than Federal Income	56,665
Federal Income Tax	38,714
Deferred Income Taxes	767
Income Taxes Deferred in Prior Years	(261)
Investment Tax Credit Adjustment	12,741
Total Operating Revenue Deductions	$349,357

The Commission finds total operating revenue deductions of $349,357, as presented by the Applicant, to be the proper amount.

18. Operating Income is found to be $129,406:

Operating Revenue	$478,763
Operating Deductions	349,357
Operating Income	$129,406

19. Rate Base	$1,812,500
Rate of Return	10.95%
Return Requirement	$198,469
Adjusted Balance Available for Return	$129,406
Revenue Deficiency	$ 69,063

In order to produce a return of 10.95% on the Applicant's average original cost depreciated rate base, the Applicant will require additional annual revenues in the amount of $69,063 from its Libby, Montana water utility.

RATE DESIGN

20. The Applicant presented a cost of service study utilizing the base extra capacity method. In the base-extra capacity method, all costs are separated into components of base cost, extra capacity cost, and customer cost.

21. In the base-extra capacity cost allocation, each component of the water-system's capital cost and operating cost, relating to demand, is assigned to a demand criteria - average annual consumption, maximum day demand or maximum hour demand through utilization of a linear equation. Customer costs are assigned directly because those costs are incurred irrespective of the amount of water used.

22. The Commission, in numerous proceedings, has accepted the use of the base-extra capacity costing formula and found it to be a reasonable method for use in developing cost-based rates. In the base-extra capacity method, the accuracy of the cost of service information is very dependent upon the availability of reliable consumption data, because demand characteristics are primary allocation factors used for the assignment of cost responsibility.

23. The cost-of-service study presented to the Commission in this Docket had only one verifiable demand characteristic, that being average annual daily consumption. Other demand characteristics, maximum day demand and maximum hour demand were computed by application of a capacity factor to average daily consumption. Total maximum daily demand is an obtainable and verifiable consumption characteristic and should be a known quantity before attempting to use the base-extra capacity method of costing because of the importance of demand characteristics in

insuring proper allocation of cost responsibility. If the demand characteristics are not representative of the utility's operating experience then the results of the cost-of-service study will skewed; therefore, the Commission does not accept the Applicant's calculated maximum daily demand as definitive, especially when an actual figure is obtainable and should be used to insure proper allocation of costs and will be available for future proceedings.

24. The Commission, based upon the preceding Finding of Fact, finds that the Applicant's cost-of-service study should be rejected as a definitive statement of class revenue requirements. The Commission does find, however, that the cost study can be utilized as an indicator for determining class revenue requirements and will use it, as such, in its findings on rate design. RESIDENTIAL RATES

25. For Rate Schedule 63, Residential Water Service, the Applicant's proposed rate structure includes a minimum charge with 3,000 gallons minimum consumption and a two-block declining commodity charge. Late-Filed Exhibit 3L-4a contains the revised rates proposed by the Applicant which are designed to generate annual revenues of $333,213 from the residential customer class.

26. In order No. 4946a, the Commission stated "that in the next general rate increase proceeding before this Commission, the Applicant should present sufficient information to support any proposed rate structure". The main concern of the Commission and the reason it placed the preceding requirement in that order was the existence of a 5,000 gallon minimum consumption allowance in the residential rate structure.

The Applicant, in its proposed rate structure, has reduced the minimum consumption allowance from its present level of 5,000 gallons monthly to 3,000 gallons monthly. This reduction in the minimum allowance was proposed by the Applicant in an effort to better reflect the use of low volume consumers, ie. an effort to recognize the fact that a substantial portion of the consumers connected to the water system do not consume 5,000 gallons in a one month period.

27. Billing information submitted by the Applicant, indicates that approximately 38.5% of the total bills issued to consumers connected to the Libby water system are for consumption of 3,000 gallons or less. This would indicate that the present 5,000 gallon minimum consumption allowance is excessive because 38.5% of the consumer billings are paying for water which they are not receiving. The applicant's proposal to reduce the minimum consumption allowance from 5,000 gallons monthly to 3,000 gallons monthly is reasonable and more reflective of the actual minimum consumption experienced on the system and is, therefore, accepted by the Commission.

28. The Applicant's revised Rate Schedule 63 (Exhibit 3L-4a) reflects a decreased minimum monthly charge for consumers using 3,000 gallons or less per month and was developed by using data from the cost-of-service study. The Commission, in Finding of Fact No. 24, rejected the Applicant's cost-of-service study, therefore, the Commission rejects the minimum monthly charges calculated using that data.
The Commission is concerned that if there are inherent errors in the Applicant's cost-of-service study, then allowing a reduction in the minimum monthly charge at this time may give the consumer a false pricing signal and possibly result in severe customer impact when those errors are corrected. The Commission is of the opinion that the more moderate policy of leaving minimum monthly charges at their present level, with the modified consumption allowance, and adjusting the minimum monthly charge when it has fully developed cost-of-service study is appropriate.

29. The minimum monthly charge, as revised by the Commission, will generate total revenues in the amount of $263,449 (17,355 billings x 15.18 minimum charge = $263,449). The remaining revenue requirement for the residential customer class using the

information from the Applicant's cost-of-service study, equals $74,764 ($338,213 - 263,449 = $74,764) and it is proposed that it be recovered through a commodity charge.

30. The Commission, in a previous finding, stated that it rejected the Applicant's cost-of-service study as definitive, but would use it as an indicator for purposes of determining class revenue requirement. The Commission's examination of data submitted in support of the Applicant's proposed water rate adjustment revealed that the Commercial and Industrial Customer class's total annual water consumption approximated 94% (82,042 , 87,484 = 93.8%) of the residential class's total annual water consumption, while their revenue contribution toward the overall requirement of the water utility equaled only approximately 53% (159,997 , 299,343 = 53.4%) of the residential class's revenue contribution, under present and proposed rates.

The Commission is cognizant of the fact that many variables enter into the proper setting of rates for various customer classifications and that the Applicant's cost-of-service study, as presented, supports the Applicant's proposed class revenue requirements at the consumption levels presented. But

the comparative disparities presented in the preceding paragraph are of grave concern to the Commission and absent a fully credible cost-of-service study, the Commission finds it appropriate to adjust the class revenue requirements of the Residential and Commercial-Industrial. The Commission is of the opinion that the Commercial-Industrial class revenue requirement should be increased, thus reducing the comparative disparity between the revenue contribution on comparable water consumption.

31. The Applicant has proposed that a two-block declining commodity charge be implemented to recover the remaining revenue requirement of the residential customer class. The Applicant's witness, Lyle Kammerer, stated during his testimony that no cost justification existed that supported the implementation of a declining block rate schedule for the residential customer class.

The Commission concurs with the witness's statement and, therefore rejects implementation of a declining block rate schedule.

32. At the present time, the Applicant has in effect a commodity charge of $1.38 per thousand gallons for all consumption in excess of that allowed in the minimum charge. With the modification in the minimum consumption allowance authorized, reducing it from 5,000 gallons monthly to 3,000 gallons monthly, and leaving the commodity charge at its present level, the Applicant will realize total annual revenues from the commodity charge of $62,645, representing an annual revenue increase in the amount of $26,751 from the residential customer class.

The Commission is of the opinion, given the disparity between the comparative revenue contribution of the Residential and Commercial-Industrial customer class and in an effort to minimize customer impact, as well as enable residential customers to continue irrigation, that the commodity charge for residential consumers should not be modified. The Commission finds that the presently existing commodity charge for residential consumers should not be changed and that the balance of the proposed revenue increase, amounting to $12,119, not realized from increased rates to the residential class should be transferred to the Commercial-Industrial customer class.

COMMERCIAL RATES

33. For Rate Schedule 66, Commercial and Industrial Water Service, the Applicant's proposed rate structure includes a minimum charge with a minimum consumption allowance based upon meter size and a three block declining commodity charge. Late-Filed Exhibit 3L-5a contains the revised rates proposed by the Applicant which are designed to generate annual revenues of $180,819 from the commercial-industrial customer class. With the Commission's requirement in Finding of Fact No. 32 that the Commercial Industrial class's revenue contribution be increased by $12,119, it will be necessary for the Commission to make findings adjusting the

Commercial-Industrial Rate Schedule 66.

34. The Applicant's revised Rate Schedule 66 (Exhibit 3L-5a) reflects a decreased minimum monthly charge for certain consumers using less than the minimum monthly consumption allowance, specifically chose consumers with a 3/4 inch and 1 inch meter, all other minimum monthly charges reflect an increase. The minimum monthly charges were developed by using data from the cost-of-service study which, as previously stated, has been rejected by the Commission. Therefore, the Commission finds it appropriate to make adjustments to the Applicant's proposed minimum monthly charges.

35. The Commission is of the opinion that the proposed reduction in the minimum monthly charge for the 3/4 inch and 1 inch metered customer should be denied for the reasons stated in Finding of Fact No. 28 and that the Applicant should maintain its current pricing policy and set those minimums at the level approved for the comparable meter size on the residential rate schedule.
Relative to the establishment of increased minimum monthly charges for all other meter sizes on Rate Schedule 66 the Commission finds this to be acceptable. It has been the Commission's experience, generally, that consumers having meters exceeding 1 inch in size normally exceed the minimum consumption allowances established. Therefore, minimal customer impact could be expected from increased minimum charges on larger meter sizes.

36. The preceding adjustments, to the Applicant's minimum monthly charges, have a negligible effect on revenue generated from the Commercial-Industrial rate schedule, therefore, it will be necessary for the Commission to adjust the Applicant's proposed commodity charges to generate the additional $12,119 in revenue requirements attributed to this customer class.

37. If the Commission increases the commodity charge in block 1, this will cause a lower minimum monthly consumption allowance, because the minimum monthly consumption allowance is determined by

dividing the approved minimum monthly charge by the rate in block 1 and this would operate to increase consumption in block 1 and possibly cause the generation of excess revenues. Therefore, the Commission has determined that the additional revenue requirement for the Commercial-Industrial class should be generated by increasing the commodity charge in blocks 2 and 3. The Commission understands (based on Commission staff/Company communications) that the least customer impact, from this rate revision, occurs when the increased revenue requirement is generated by a uniform cost per thousand gallon increase in blocks 2 and 3. The Commission finds that the Applicant should increase the commodity charge in blocks 2 and 3 by $.19 per thousand gallons ($12,119 ,' 63,111 M gal. in blocks 2 & 3 = $.192).

38. All other rate design proposals not discussed herein are approved, as reflected in Late-Filed Exhibit 3L-1, including the cancellation of Schedule 67.

MISCELLANEOUS

39. Concern was expressed during the public hearing relative to customer/company responsibility regarding prevention of freezing and thawing of pipes. The Company's tariff at rules 6(h) and 6(i) address these concerns and the Commission is of the opinion that these rules as presently approved provide adequate protection and assignment of responsibility.

CONCLUSIONS OF LAW

1. The Montana Public Service Commission properly exercises jurisdiction over the parties and subject matter in this proceeding. Section 69-3-102, MCA.

2. The Commission afforded all interested parties in this proceeding proper notice and an opportunity to participate. Section 69-3-303, MCA.

The rates approved herein are reasonable, just and proper. Section 69-3-201, MCA.

ORDER

THEREFORE, THE MONTANA PUBLIC SERVICE COMMISSION ORDERS THAT:

1. Pacific Power and Light Company shall file tariffs, consistent with the Findings of Fact herein, which reflect an increase in annual revenues of $69,063 for its Libby, Montana service area.

2. The rates approved herein shall be effective for water service rendered on and after June 4, 1984.

3. A full, true and correct copy of this Order shall be sent forthwith by first-class United States mail to the Applicant and all other appearances herein.

DONE IN OPEN SESSION this 4th day of June, 1984 by a vote of 4 to 0.

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION.

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Howard L. Ellis, Commissioner

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Danny Oberg, Commissioner

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John B Driscoll, Commissioner

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Clyde Jarvis, Commissioner

ATTEST:

Madeline L. Cottrill
Commission Secretary

(SEAL)

NOTE: Any interested party may request the Commission to reconsider this decision. A motion to reconsider must be filed within ten (10) days. See 38.2.4806, ARM.